

**Memorandum**

JUL 18 2000

Date

From

*Michael Mangano*June Gibbs Brown  
Inspector General

Subject

Review of Medicare Contractor's Pension Segmentation, General American Life Insurance Company (A-07-99-02540)

To

Nancy-Ann Min DeParle  
Administrator  
Health Care Financing Administration

This memorandum is to alert you to the issuance on Thursday, July 20, 2000, of our final audit report identifying about \$6.2 million of Medicare segment pension assets at General American Life Insurance Company (General American) which had not previously been identified. A copy is attached and copies of the report have been distributed to your staff for adjudication of the finding.

General American administered Medicare Part B under cost reimbursement contracts since the start of the Medicare program. Beginning with Fiscal Year 1988, the Health Care Financing Administration incorporated pension segmentation requirements into Medicare contracts. The contractual language specifies segmentation requirements and also provides for the separate identification of the pension assets for a Medicare segment.

Our review showed that General American understated the Medicare segment pension assets as of January 1, 1988 by \$259,101. The understatement occurred primarily because General American omitted certain Medicare segment participants in determining Medicare's initial assets. We also found that General American did not update the Medicare segment pension assets beyond January 1, 1988.

We computed General American's update of Medicare segment pension assets from 1988 to 1998. We determined the Medicare segment pension assets to be \$6,205,564 as of January 1, 1998. Accordingly, we are recommending that General American identify Medicare segment pension assets of \$6,205,564 as of January 1, 1998. General American agreed with the finding and recommendation.

If you need additional information about this report, please contact Barbara A. Bennett, Regional Inspector General for Audit Services, Region VII, 816-426-3591.

Attachment

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF MEDICARE  
CONTRACTOR'S PENSION  
SEGMENTATION, GENERAL  
AMERICAN LIFE INSURANCE  
COMPANY**



**JUNE GIBBS BROWN  
Inspector General**

**JULY 2000  
A-07-99-02540**



## DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General  
Office of Audit Services

Region VII  
601 East 12<sup>th</sup> Street  
Room 284A  
Kansas City, Missouri 64106

CIN A-07-99-02540

Mr. Walter Schultz  
Group Information Systems VP  
GenAmerica Corporation - F1-40  
Post Office Box 14490  
St. Louis, Missouri 63178

Dear Mr. Schultz:

This report provides you with the results of the Office of Inspector General (OIG), Office of Audit Services (OAS) review entitled, *Review of Medicare Contractor's Pension Segmentation, General American Life Insurance Company*. The purpose of our review was to evaluate General American Life Insurance Company's (General American) compliance with the pension segmentation requirements of its Medicare contract.

Our review showed that General American understated the Medicare segment pension assets as of 1986 by \$220,185. The understatement occurred primarily because General American omitted certain Medicare segment participants in determining Medicare's initial assets. Additionally, General American's update for the Medicare segment assets from Plan Year 1986 to Plan Year 1988 understated segment assets by \$38,916. This understatement occurred because General American started the update with an understated asset base. General American did not update the Medicare segment pension assets beyond January 1, 1988. We computed General American's update of Medicare segment pension assets from 1988 to 1998.

We recommend that General American identify Medicare segment pension assets of \$6,205,564 as of January 1, 1998. General American agreed with our finding. General American's response is included in its entirety as APPENDIX B.

## INTRODUCTION

### BACKGROUND

General American administered Medicare Part B under cost reimbursement contracts since the start of the Medicare program. The contracts, the Federal Acquisition Regulations (FAR), which

superseded the Federal Procurement Regulations (FPR), and the Cost Accounting Standards (CAS) contain reimbursement principles for cost reimbursement contracts.

Since its inception, Medicare has paid a portion of the annual contributions made by contractors to their pension plans. These payments represented allowable pension costs under the FPR and/or the FAR. In 1980, both the FPR and Medicare contracts incorporated CAS 412 and 413.

The CAS 412 regulates the determination and measurement of the components of pension costs. It also regulates the assignment of pension costs to appropriate accounting periods. The CAS 413 regulates the valuation of pension assets, allocation of pension costs to segments of an organization, adjustment of pension costs for actuarial gains and losses, and assignment of gains and losses to cost accounting periods.

The Health Care Financing Administration (HCFA) incorporated segmentation requirements into Medicare contracts starting with Fiscal Year 1988. The contractual language specifies segmentation requirements and also provides for the separate identification of the pension assets for a Medicare segment.

General American's contract required (1) computing the Medicare segment's actuarial liability, (2) determining the ratio of the Medicare segment's actuarial liability to the total plan actuarial liability (asset fraction), (3) allocating a portion of total pension assets as of 1986 based on the above ratio, (4) updating Medicare pension assets annually, and (5) assessing if Medicare's pension costs should be separately calculated.

The Medicare contracts identify a Medicare segment as:

“...any organizational component of the contractor, such as a division, department, or other similar subdivision, having a significant degree of responsibility and accountability for the Medicare contract/agreement, in which:

1. The majority of the salary dollars is allocated to the Medicare agreement/contract;  
or
2. Less than a majority of the salary dollars is allocated to the Medicare agreement/contract, and these salary dollars represent 40 percent or more of the total salary dollars allocated to the Medicare agreement/contract.”

The contracts also provide for separate identification of the pension assets of the Medicare segment. The identification involves the allocation of assets to the Medicare segment as of the first pension plan year after December 31, 1985 in which the salary criterion was met. The allocation was to use the ratio of the actuarial liabilities of the Medicare segment to the actuarial liabilities of the total plan, as of the later of the first day of the first plan year starting after

December 31, 1980, or the first day of the first pension plan year following the date such Medicare segment first existed.

To ensure that contractors developed and maintained the data necessary for segmentation calculations, HCFA distributed a pension cost questionnaire to contractors in 1989. General American's questionnaire response identified total pension assets of \$35,929,393 and Medicare segment assets of \$1,043,785 as of January 1, 1986.

## **OBJECTIVE, SCOPE, AND METHODOLOGY**

We made our examination in accordance with generally accepted government auditing standards. Our objective was to determine General American's compliance with pension segmentation requirements of its Medicare contract. Achieving the objective did not require a review of General American's internal control structure. The audit addressed General American's initial determination of pension assets for its Medicare segments and later updates. Our review covered January 1, 1981 to January 1, 1998.

We reviewed General American's identification of the Medicare segment as of January 1, 1988 and traced the segment's organizational lineage back to 1981. We also reviewed General American's computation of the asset fraction and its update of Medicare segment pension assets from January 1, 1986 to January 1, 1988.

In performing the review, we used information provided by General American's consulting actuarial firms. The information included liabilities, normal costs, contributions, expenses, and earnings. We reviewed General American's accounting records, pension plan documents, annual actuarial valuation reports, and the Department of Labor/Internal Revenue Service Form 5500s. Using these documents, we calculated the asset fraction, determined the 1986 Medicare segment assets, and updated the Medicare segment assets to January 1, 1998. The HCFA pension actuarial staff reviewed our methodology and calculations.

We performed site work at General American's corporate offices in St. Louis, Missouri during September and October of 1999. Subsequently, we performed audit work in our Jefferson City, Missouri office.

## **FINDING AND RECOMMENDATION**

### **MEDICARE ASSETS AS OF JANUARY 1, 1986**

We determined that General American's asset fraction was understated by .5558 percent. General American omitted 14 Medicare participants from the 1981 segment, and was unable to provide adequate support for their asset fraction computation. We increased the asset fraction from 2.9051 percent to 3.4609 percent by including the omitted participants, and by computing

the actuarial accrued liability on an individual basis. Our calculation increased the Medicare segment assets by \$220,185 to \$1,371,070.

General American provided a list of 89 participants representing the 1981 Medicare segment. However, General American was unable to provide the participants' actuarial accrued liability on an individual basis. We identified an additional 14 Medicare participants that General American had omitted from their list. Additionally, we computed the actuarial accrued liability on an individual basis for all General American pension plan participants as of January 1, 1981. We calculated General American's asset fraction using our identification of the 1981 Medicare segment participants and our computation of the actuarial accrued liability. The following schedule shows the details of General American's and our calculations.

		1981 Total Actuarial <u>Liability</u> (A)	1981 Medicare Actuarial <u>Liability</u> (B)	1981 Rounded Asset <u>Fraction</u> (C)=(B)/(A)	1986 Total Company <u>Assets 1/</u> (D)	1986 Medicare Segment <u>Assets 1/</u> (E)=(C)(D)
OIG Calculation		\$19,938,999	\$690,070	3.4609%	\$39,616,006	\$1,371,070
General American Calculation	2/	\$19,939,003	<u>\$579,256</u>	<u>2.9051%</u>	<u>\$39,616,006</u>	<u>\$1,150,885</u>
Difference				<u>0.5558%</u>	<u>\$0</u>	<u>\$220,185</u>

1/ Market Value of Assets (MVA)

2/ General American applied their asset fraction to the actuarial value of assets (AVA) in their questionnaire response. We computed the asset split and the update of segment assets (see APPENDIX A) using the MVA. For purposes of comparison we applied General American's asset fraction to the MVA in the above illustration.

#### **MEDICARE ASSET BASE AS OF JANUARY 1, 1986 UPDATED TO JANUARY 1, 1988**

General American's update of the Medicare segment assets from January 1, 1986 to January 1, 1988 understated the segment assets by \$38,916. This understatement primarily occurred because General American started the update with an understated asset base for 1986. When considered with the 1986 adjustment, General American understated Medicare's pension assets by \$259,101 as of January 1, 1988.

As of January 1, 1988, General American determined Medicare segment assets of \$1,495,463 based on the actuarial value of assets (AVA). For purposes of comparison we converted General American's determination of segment assets to the market value of assets (MVA), which were \$1,634,922 (see APPENDIX A for further details). We identified Medicare segment pension assets of \$1,894,023 as of January 1, 1988. The increase of \$259,101 resulted from: (1) revising the asset fraction (\$220,185 increase), (2) revising earnings and expenses (\$44,716 increase), and (3) adjusting benefit payments (\$5,800 decrease).

### **Earnings and Expenses**

Investment earnings and expenses were assigned to the Medicare segment based on a ratio of segment assets to total company assets. Because General American started their update with an understated asset base, it understated the segment's earnings and expenses for each year of the update. We used the corrected asset amounts in our update of the Medicare segment assets and increased the Medicare segment assets by \$44,716.

### **Benefit Payments**

Due to the incorrect identification of the Medicare segment participants, General American's update of segment assets did not properly identify benefit payments to retirees that were segment participants. We matched benefit payments to individual retirees and used these payments in updating the segment assets shown in APPENDIX A. This resulted in a net decrease of \$5,800 in the Medicare segment assets.

### **MEDICARE ASSET BASE AS OF JANUARY 1, 1988 UPDATED TO JANUARY 1, 1998**

General American did not update the Medicare segment assets from January 1, 1988 to January 1, 1998. Using information provided by General American, we calculated the update of segment assets from January 1, 1988 to January 1, 1998. See APPENDIX A. We determined Medicare segment pension assets to be \$6,205,564 as of January 1, 1998.

### **Recommendation:**

We recommend that General American:

Identify pension assets of \$6,205,564 for the Medicare segment as of January 1, 1998.

### **Auditee Response**

Initially, General American disagreed with our finding and submitted additional documentation supporting their position. After analyzing the additional information, we revised our computations and finding. Subsequently, General American agreed with our revised finding. General American's response is included in its entirety as APPENDIX B.

### **OIG Comments**

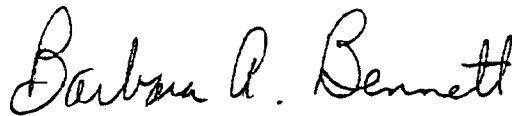
All amounts set forth in this report reflect the revisions agreed to by General American.

### INSTRUCTIONS FOR AUDITEE RESPONSE

Final determinations as to actions to be taken on all matters reported will be made by the HHS action official identified below. We request that you respond to the recommendation in this report within 30 days from the date of this report to the HHS action official, presenting any comments or additional information that you believe may have a bearing on final determination.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG, OAS, reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise.  
(See 45 CFR Part 5.)

Sincerely,

A handwritten signature in black ink that reads "Barbara A. Bennett". The signature is written in a cursive, flowing style.

Barbara A. Bennett  
Regional Inspector General for  
Audit Services, Region VII

Enclosures

HHS Action Official:

Mr. Joe L. Tilghman  
Regional Administrator, Region VII  
Health Care Financing Administration  
601 E. 12<sup>th</sup> Street, Room 235  
Kansas City, Missouri 64106



GENERAL AMERICAN LIFE INSURANCE CO.  
CIN A-07-99-02540

STATEMENT OF MEDICARE PENSION ASSETS  
JANUARY 1, 1986 TO JANUARY 1, 1998

Asset Fraction, January 1, 1981: 3.4609%

Date	Description	Total Company	Other Segment	Medicare Segment
01/01/1986	Market Value of Assets 1/	\$39,616,006	\$ 38,244,936	\$1,371,070
	Employer Contribution 2/	3,506,893	3,372,002	134,891
	Investment Return 3/	5,154,074	4,975,697	178,377
	Benefit Payments 4/	(707,890)	(696,003)	(11,887)
	Administrative Expenses 5/	<u>(69,364)</u>	<u>(66,963)</u>	<u>(2,401)</u>
01/01/1987	Market Value of Assets	47,499,719	45,829,669	1,670,050
	Employer Contribution	3,106,971	3,021,035	85,936
	Investment Return	4,480,422	4,322,894	157,528
	Benefit Payments	(886,216)	(872,206)	(14,010)
	Administrative Expenses	<u>(155,877)</u>	<u>(150,396)</u>	<u>(5,481)</u>
01/01/1988	Market Value of Assets *	54,045,019	52,150,996	1,894,023
* Assets January 1, 1988 6/				
	Assets Per General American	\$54,045,019	\$52,150,996	\$1,894,023
	Variance	\$0	(\$259,101)	\$259,101
	Employer Contribution	0	0	0
	Investment Return	6,142,147	5,926,894	215,253
	Benefit Payments	(1,071,886)	(1,051,967)	(19,919)
	Administrative Expenses	<u>(170,904)</u>	<u>(164,915)</u>	<u>(5,989)</u>
01/01/1989	Market Value of Assets	58,944,376	56,861,008	2,083,368
	Employer Contribution	0	0	0
	Investment Return	14,218,926	13,716,363	502,563
	Benefit Payments	(1,248,898)	(1,231,684)	(17,214)
	Administrative Expenses	<u>(310,700)</u>	<u>(299,718)</u>	<u>(10,982)</u>
01/01/1990	Market Value of Assets	\$ 71,603,704	\$ 69,045,969	\$ 2,557,735

GENERAL AMERICAN LIFE INSURANCE CO.  
CIN A-07-99-02540

STATEMENT OF MEDICARE PENSION ASSETS  
JANUARY 1, 1986 TO JANUARY 1, 1998

Date	Description	Total Company	Other Segment	Medicare Segment
01/01/1990	Market Value of Assets	\$ 71,603,704	\$ 69,045,969	\$ 2,557,735
	Employer Contribution	0	0	0
	Investment Return	(1,211,646)	(1,168,365)	(43,281)
	Benefit Payments	(1,487,152)	(1,467,104)	(20,048)
	Administrative Expenses	<u>(305,445)</u>	<u>(294,534)</u>	<u>(10,911)</u>
01/01/1991	Market Value of Assets	68,599,461	66,115,966	2,483,495
	Employer Contribution	0	0	0
	Investment Return	13,564,041	13,072,984	491,057
	Benefit Payments	(1,727,007)	(1,709,529)	(17,478)
	Administrative Expenses	<u>(319,596)</u>	<u>(308,026)</u>	<u>(11,570)</u>
01/01/1992	Market Value of Assets	80,116,899	77,171,395	2,945,504
	Employer Contribution	0	0	0
	Investment Return	8,315,601	8,009,877	305,724
	Benefit Payments	(2,073,376)	(2,056,790)	(16,586)
	Administrative Expenses	<u>(302,684)</u>	<u>(291,556)</u>	<u>(11,128)</u>
01/01/1993	Market Value of Assets	86,056,440	82,832,926	3,223,514
	Employer Contribution	0	0	0
	Investment Return	12,280,946	11,820,925	460,021
	Benefit Payments	(2,371,375)	(2,352,774)	(18,601)
	Administrative Expenses	<u>(374,688)</u>	<u>(360,653)</u>	<u>(14,035)</u>
01/01/1994	Market Value of Assets	95,591,323	91,940,424	3,650,899
	Employer Contribution	0	0	0
	Investment Return	(2,755,759)	(2,650,509)	(105,250)
	Benefit Payments	(2,505,421)	(2,488,114)	(17,307)
	Administrative Expenses	<u>(405,131)</u>	<u>(389,658)</u>	<u>(15,473)</u>
01/01/1995	Market Value of Assets	\$ 89,925,012	\$ 86,412,143	\$ 3,512,869

GENERAL AMERICAN LIFE INSURANCE CO.  
CIN A-07-99-02540

STATEMENT OF MEDICARE PENSION ASSETS  
JANUARY 1, 1986 TO JANUARY 1, 1998

Date	Description	Total Company	Other Segment	Medicare Segment
01/01/1995	Market Value of Assets	\$ 89,925,012	\$ 86,412,143	\$ 3,512,869
	Employer Contribution	0	0	0
	Investment Return	28,373,764	27,265,359	1,108,405
	Benefit Payments	(2,985,670)	(2,945,379)	(40,291)
	Administrative Expenses	<u>(388,824)</u>	<u>(373,635)</u>	<u>(15,189)</u>
01/01/1996	Market Value of Assets	114,924,282	110,358,488	4,565,794
	Employer Contribution	35,085	35,085	0
	Investment Return	14,694,670	14,110,870	583,800
	Benefit Payments	(3,388,750)	(3,352,707)	(36,043)
	Administrative Expenses	<u>(544,256)</u>	<u>(522,633)</u>	<u>(21,623)</u>
01/01/1997	Market Value of Assets	125,721,031	120,629,103	5,091,928
	Employer Contribution	28,786	28,786	0
	Investment Return	29,683,617	28,481,377	1,202,240
	Benefit Payments	(4,322,338)	(4,258,467)	(63,871)
	Administrative Expenses	<u>(610,652)</u>	<u>(585,919)</u>	<u>(24,733)</u>
01/01/1998	Market Value of Assets	<u>\$ 150,500,444</u>	<u>\$ 144,294,880</u>	<u>\$ 6,205,564</u>

*GENERAL AMERICAN LIFE INSURANCE CO.*  
*CIN A-07-99-02540*

**STATEMENT OF MEDICARE PENSION ASSETS**  
**JANUARY 1, 1986 TO JANUARY 1, 1998**

1/ We calculated the Medicare segment assets based on our identification of the Medicare segment and our computed asset fraction (3.4609%). We computed the asset fraction as explained in our finding section of the report narrative. The amounts shown for the other segment represent the difference between the total company and the Medicare segment. All pension assets are shown at MVA.

2/ We obtained total contribution amounts from IRS Form 5500 reports. General American did not make contributions to the pension trust fund for plan years 1988 through 1995. Additionally, the contributions made for plan years 1996 through 1998 were totally attributable to the "other" segment. Therefore, no portion of these years' contributions were assigned to the Medicare segment. For plan years 1986 and 1987, we assigned contributions to the Medicare segment in the same amount as identified by General American.

3/ We obtained the total investment return from actuarial valuation reports. We allocated investment return to the Medicare segment based on the ratio of Medicare segment assets to total company assets.

4/ We obtained total benefit payments from actuarial valuation reports. We based the Medicare segment's benefit payments on actual payments to Medicare retirees.

5/ We obtained total plan expenses from actuarial valuation reports. We allocated expenses to the segment based on the ratio of Medicare segment assets to total company assets.

6/ General American calculated the asset split and update of segment assets using the AVA. In their questionnaire response, General American identified Medicare segment pension assets of \$1,495,463 (AVA) as of January 1, 1988. For purposes of comparison, we converted the segment's AVA to the MVA based on the ratio of the total company AVA to the total company MVA.

John W. Barber, CPA, FLMI/M  
*Vice President  
and Controller*

April 12, 2000

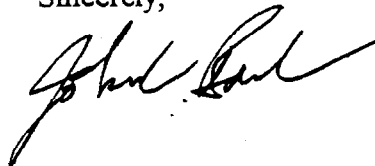
Ms. Barbara A. Bennett  
Regional Inspector General  
for Audit Services, Region VII  
601 East 12th Street, Room 284A  
Kansas City, MO 64106

Dear Ms. Bennett:

CIN: A-07-99-02540

We did not agree with the November, 1999 draft audit report recommendation on the value of the pension assets. Subsequent evaluations between Wm. M. Mercer, Inc. representatives on our behalf with Mr. Eric Shipley resulted in an agreement with which we concur. Specifically, we agree with the Medicare segment pension asset fraction of 3.4609% at January 1, 1981 and assets of \$6,205,564 at January 1, 1998.

Sincerely,



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